

Culture for a digital age

Risk aversion, weak customer focus, and siloed mind-sets have long bedeviled organizations. In a digital world, solving these cultural problems is no longer optional.

by Julie Goran, Laura LaBerge, and Ramesh Srinivasan

Shortcomings in organizational culture are one of the main barriers to company success in the digital age. That is a central finding from McKinsey's recent survey of global executives (Exhibit 1), which highlighted three digital-culture deficiencies: functional and departmental silos, a fear of taking risks, and difficulty forming and acting on a single view of the customer.

Each obstacle is a long-standing difficulty that has become more costly in the digital age. When risk aversion holds sway, underinvestment in strategic opportunities and sluggish responses to quick-changing customer needs and market dynamics can be the result.¹ When a unified understanding of customers is lacking, companies struggle to mobilize employees around integrated touchpoints, journeys, and consistent experiences, while often failing to discern where to best place their bets as digital broadens customer choice and the actions companies can take in response. And when silos characterize the organization, responses to rapidly evolving customer needs are often too narrow, with key signals missed or acted upon too slowly, simply because they were seen by the wrong part of the company.

Can fixes to culture be made directly? Or does cultural change emerge as a matter of course as executives work to update strategy or improve processes?²

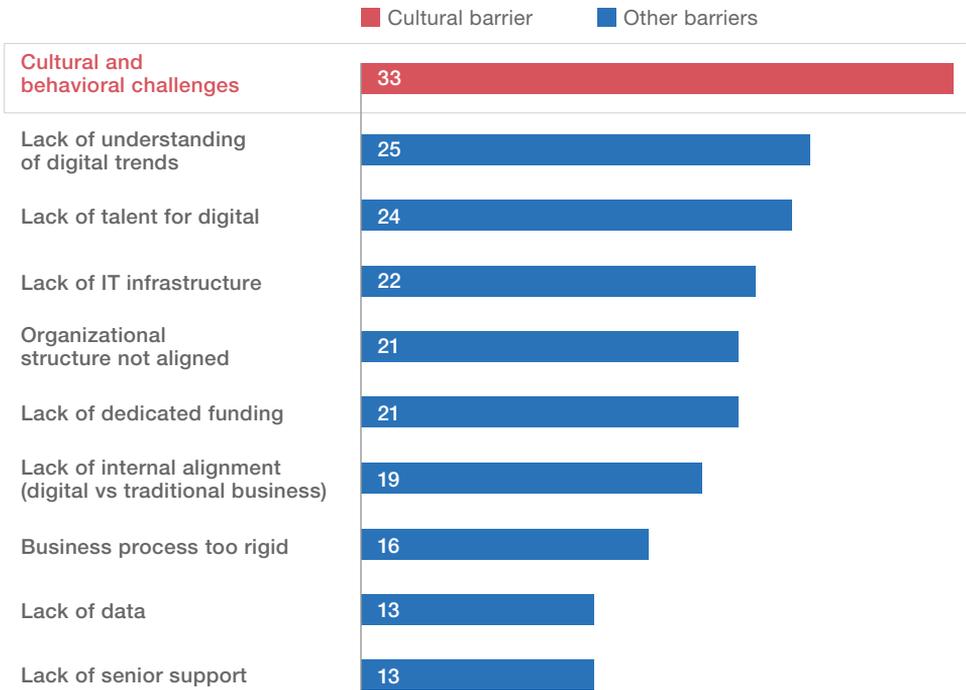
¹ See Tim Koller, Dan Lovallo, and Zane Williams, "Overcoming a bias against risk," August 2012, McKinsey.com.

² Jay W. Lorsch and Emily McTague argue for culture emerging indirectly in "Culture is not the culprit," *Harvard Business Review*, April 2016, Volume 94, Number 4, pp. 96–105, hbr.org.

Exhibit 1

Culture is the most significant self-reported barrier to digital effectiveness.

Which are the most significant challenges to meeting digital priorities?
% of respondents



McKinsey&Company | Source: 2016 McKinsey Digital survey of 2,135 respondents

In our experience, executives who wait for organizational cultures to change organically will move too slowly as digital penetration grows, blurs the boundaries between sectors (see “Competing in a world of sectors without borders,” on McKinsey.com), and boosts competitive intensity. Our research, which shows that cultural obstacles correlate clearly with negative economic performance (Exhibit 2), supports this view. So do the experiences of leading players such as BBVA, GE, and Nordstrom, which have shown what it looks like when companies support their digital strategies and investments with deliberate efforts to make their cultures more responsive to customers, more willing to take risks, and better connected across functions.

Executives must be proactive in shaping and measuring culture, approaching it with the same rigor and discipline with which they tackle operational transformations. This includes changing structural and tactical elements in an organization that run counter to the culture change they are trying to achieve. The critical cultural intervention points identified by respondents

to our 2016 digital survey—risk aversion, customer focus, and silos—are a valuable road map for leaders seeking to persevere in reshaping their organization’s culture. The remainder of this article discusses each of these challenges in turn, spelling out a focused set of reinforcing practices to jump-start change.

CALCULATED RISKS

Too often, management writers talk about risk in broad-brush terms, suggesting that if executives simply encourage experimentation and don’t punish failure, everything will take care of itself. But risk and failure profoundly challenge us as human beings. As Ed Catmull of Pixar said in a 2016 *McKinsey Quarterly* interview, “One of the things about failure is that it’s asymmetrical with respect to time. When you look back and see failure, you say, ‘It made me what I am!’ But looking forward, you think, ‘I don’t know what is going to happen and I don’t want to fail.’ The difficulty is that when you’re running an experiment, it’s forward looking. We have to try extra hard to make it safe to fail.”³

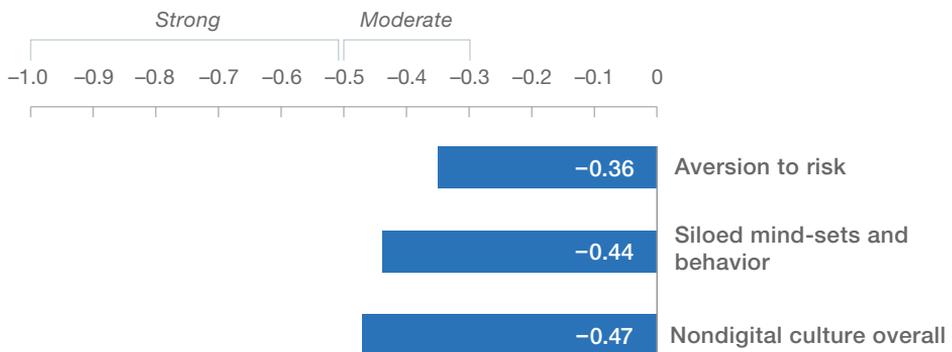
The balancing act Catmull described applies to companies, perhaps even more than to individuals. Capital markets have typically been averse to investments that are hard to understand, that underperform, or that take

³ See “Staying one step ahead at Pixar: An interview with Ed Catmull,” *McKinsey Quarterly*, March 2016, McKinsey.com.

Exhibit 2

Cultural obstacles correlate clearly with negative economic performance.

Negative correlation with economic performance
(correlation coefficient)



McKinsey&Company | Source: 2016 McKinsey Digital survey of 2,135 respondents

a long time to reach fruition. And the digital era has complicated matters: On the one hand, willingness to experiment, adapt, and to invest in new, potentially risky areas has become critically important. On the other, taking risks has become more frightening because transparency is greater, competitive advantage is less durable, and the cost of failure is high, given the prevalence of winner-take-all dynamics.⁴

Leaders hoping to strike the right balance have two critical priorities that are mutually reinforcing at a time when fast-follower strategies have become less safe. One is to embed a mind-set of risk taking and innovation through all ranks of the enterprise. The second is for executives themselves to act boldly once they have decided on a specific digital play—which may well require changing mind-sets about risk, and inspiring key executives and boards to think more like venture capitalists.

An appetite for risk

Building a culture where people feel comfortable trying things that might fail starts with senior leaders' attitudes and role modeling. They must break the status quo of hierarchical decision making, overcome a focus on optimizing rather than innovating, and celebrate learning from failure. It helps considerably when executives make it clear through actions that they trust the front lines to make meaningful decisions. ING and several other companies have tackled this imperative head-on, providing agile coaches to help management learn how to get out of the way after setting overall direction for objectives, budgets, and timing.⁵

However, delegating authority only works if the employees have the skills, mind-sets, and information access to make good on it. Outside hires from start-ups or established digital natives can help inject disruptive thinking that is a source of innovative energy and empowerment. Starbucks, for example, has launched a digital-ventures team, hiring vice presidents from Google, Microsoft, and Razorfish to help drive outside thinking.

Also empowering for frontline workers (and risk dampening for organizations) is information itself. For example, equipping call-center employees with real-time analysis on account profiles, or data on usage and profitability, helps them take small-scale risks as they modify offers and adjust targeting in real time. In the retail and hospitality industries,

⁴ See Jacques Bughin, Laura LaBerge, and Anette Mellbye, "The case for digital reinvention," *McKinsey Quarterly*, February 2017, McKinsey.com.

⁵ See "ING's agile transformation," *McKinsey Quarterly*, January 2017, McKinsey.com.

companies are giving frontline employees both the information (such as segment and purchase history) and the decision authority they need to resolve customer issues on the spot, without having to escalate to management. Such information helps connect the front line to the company's strategic vision, which provides a compass for decision making on things such as what sort of discount or incentive to offer in resolving a conflict or what "next product to buy" to tee up. Benefits include improvements in the customer experiences (due to faster resolution) and greater consistency across the business in spotting and resolving problems. This lowers cost at the same time it improves customer satisfaction. In addition, frontline risk taking enables more rapid innovation by speeding up iterations and decision making to support nimbler, test-and-learn approaches. These same dynamics prevail in manufacturing, with new algorithms enabling predictive maintenance that no longer requires sign-off from higher-level managers.

Regardless of industry, the critical question for executives concerned with their organization's risk appetite is whether they are trusting their employees, at all levels, to make big enough bets without subjecting them to red tape. Many CFOs have decided to shift all but the largest investment decisions into the business units to speed up the process. The CFO at one global 500 consumer-goods company now signs off only on expenditures above \$250,000. Until recently, any spend decision over \$1,000 required the CFO's approval.

Making bold bets

At the same time they are letting go of some decisions, senior leaders also are responsible for driving bold, decisive actions that enable the business to pivot rapidly, sometimes at very large scale. Such moves require risk taking, including aggressive goal setting and nimble resource reallocation.

A culture of digital aspirations. Goals should reflect the pace of disruption in a company's industry. The *New York Times* set the aspiration to double its digital revenues within five years, enabled in part by the launch of T Brand Studio as a new business model. In the face of Amazon, Nordstrom committed more than \$1.4 billion in technology capital investments to enable rich cross-channel experiences. The Irish bank AIB decided customers should be able to open an account in under ten minutes (90 percent faster than the norm prevailing at the time). AIB invested to achieve this goal and saw a 25 percent lift in accounts opened, along with a 20 percent drop in costs. In many industries facing digital disruption, this is the pace and scale at which executives need to be willing to play.

Embracing resource reallocation. Nimble resource reallocation is typically needed to back up such goals. In many incumbents, though, M&A and capital-expenditure decisions are too slow, with too many roadblocks in the way. They need to be retooled to take on more of a venture-capitalist approach to rapid sizing, testing, investing, and disinvesting. The top teams at a large global financial-services player and an IT-services company have been reevaluating all of their businesses with a five- to ten-year time horizon, determining which ones they will need to exit, where they need to invest, and where they can stay the course. Such moves tax the risk capacity of executives; but when the moves are made, they also shake things up and move the needle on a company's risk culture.

The financial markets are double-edged swords when it comes to bold moves. While they remain preoccupied with short-term earnings, they are also cognizant of cautionary tales such as Blockbuster's 2010 bankruptcy, just three years after the launch of Netflix's streaming-video business. Companies like GE have nonetheless plunged ahead with long-term, digitally oriented strategies. In aggressively shedding some of its traditional business units, investing significantly to build out its Predix platform, and launching GE Digital, its first new business unit in 75 years, with more than \$1 billion invested in 2016, GE's top team has embraced disciplined risk taking while building for the future.

CUSTOMERS, CUSTOMERS, CUSTOMERS

Although companies have long declared their intention to get close to their customers, the digital age is forcing them to actually do it, as well as providing them with better means to do so. Accustomed to best-in-class user experiences both on- and off-line with companies such as Amazon and Apple, customers increasingly expect companies to respond swiftly to inquiries, to customize products and services seamlessly, and to provide easy access to the information customers need, when they need it.

A customer-centric organizational culture, in other words, is more than merely a good thing—it's becoming a matter of survival. The good news is that getting closer to your customers can help reduce the risk of experimentation (as customers help cocreate products through open innovation) and support fast-paced change. Rather than having to guess what's working in a given product or service before launching it—and then waiting to see if your guess is right after the launch takes place—companies can now make adjustments nearly real-time by developing product and service features with direct input from end users. This is already taking place in products from Legos

to aircraft engines. The process not only helps derisk product development, it tightens the relationship between companies and their customers, often providing valuable proprietary data and insights about how customers think about and use the products or services being created.

Data and tools

Underlying the new customer-centricity are diverse tools and data. Connecting the right data to the right decisions can help build a common understanding of customer needs into an organizational culture, fostering a virtuous cycle that reinforces customer-centricity. Amazon's ability to use customers' previous purchases to offer them additional items in which they might be interested is a significant element in its success. The virtuous circle they've created includes customer reviews (to reassure and reinforce other shoppers), along with the algorithms that share "what customers who looked at this item also bought." Of course, Amazon has also invested heavily in automated warehouses and a sophisticated distribution model. But even those were tied to the customer desire to receive merchandise faster.

A unifying force

At its best, customer-centricity extends far beyond marketing and product design to become a unifying cultural element that drives all core decisions across all areas of the business. That includes operations, where in many organizations it's often the furthest from view, and strategy, which must be regularly refreshed if it is to serve as a reliable guide in today's rapidly changing environment. Customer-centric cultures anticipate emerging patterns in the behavior of customers and tailor relevant interactions with them by dynamically integrating structured data, such as demographics and purchase history, with unstructured data, such as social media and voice analytics.

The insurance company Progressive illustrates the unifying role played by strong customer focus. Progressive's ability to persuade customers to install the company's Snapshot device to monitor driving behavior is revolutionizing the insurance space, and not just as a marketing tool. Snapshot helps attract the good drivers who are the most profitable customers, since those individuals are the ones most likely to be attracted by the offer of better discounts based on driving behavior. It also gives the company's underwriters actual data in place of models and guesswork. This new technology is one that Progressive can monetize into a business unit to serve other insurers as well.

BUSTING SILOS

Some observers might consider organizational silos—so named for parallel parts of the org chart that don't intersect—a structural issue rather than a cultural one. But silos are more than just lines and boxes. The narrow, parochial mentality of workers who hesitate to share information or collaborate across functions and departments can be corrosive to organizational culture.

Silos are a perennial problem that have become more costly because, in the words of Cognizant CEO Francisco D'Souza, “the interdisciplinary requirement of digital continues to grow. The possibilities created by combining data science, design, and human science underscore the importance both of working cross-functionally and of driving customer-centricity into the everyday operations of the business. Many organizations have yet to unlock that potential.”⁶ The executives we surveyed appeared to agree, ranking siloed thinking and behavior number one among obstacles to a healthy digital culture.

How can you tell if your own organization is too siloed? Discussions with CEOs who have led old-line companies through successful digital transformations indicate two primary symptoms: inadequate information, and insufficient accountability or coordination on enterprise-wide initiatives.

Getting informed

Digital information breakdowns echo the familiar story of the blind men and the elephant. When employees lack insight into the broader context in which a business competes, they are less likely to recognize the threat of disruption or digital opportunity when they see it and to know when the rest of the organization should be alerted. They can only interpret what they encounter through the lens of their own narrow area of endeavor.

The corollary to this is that every part of the organization reaches different conclusions about their digital priorities, based on incomplete or simply different information. This contributes to breaks in strategic and operating consistency that consumers are fast to spot. There isn't the luxury of time in today's digital world for each division to discover the same insight; a digital attacker or more agile incumbent is likely to swoop in before the siloed organization even knows it should be mounting a response. So the first imperative for companies looking to break out of a siloed mentality is

⁶ Francisco D'Souza in discussion with the authors, July 2016.

to inspire within employees a common sense of the overall direction and purpose of the company. Data and thoughtful management rotation often play a role.

Data-driven transparency. Data can help solve the blind-men-and-the-elephant problem. A social-services company, for instance, created a customer-engagement group to better understand how customers interact with the company's products and brands across silos—and where customers were running into difficulty. Among other things, this required close examination of how the company collected, analyzed, and distributed data across silos. The team discovered, for example, that some customers were cancelling their memberships because of the deluge of marketing outreaches they were receiving from the company. To address this, the team combined customer databases and propensity models across silos to create visibility and centralized access rights with regard to who could reach out to members and when. Among other achievements, this team:

- created segment-specific trainings that offered an integrated view of each segment's suite of needs and offerings that would meet them
- drew on information from different parts of the organization to give a more developed picture on engagement, retention, and the total number of touches associated with various segments and customers
- showed the net effect of the entire organization's activities through the customer's eyes
- embedded this information into key processes to ensure information was accessible in a cross-disciplinary way—breaking siloed viewpoints and narrow understandings of the overall business model

Management rotation. Another way to achieve better alignment on the company's direction is to rotate executives between siloed functions and business units. At the luxury retailer Nordstrom, for example, two key executives exchanged roles in 2014: Erik Nordstrom, formerly president of the company's brick-and-mortar stores, became president of Nordstrom Direct, the company's online store, while Jamie Nordstrom, formerly president of Nordstrom Direct, became president of the brick-and-mortar stores. This type of rotation can be done at different levels in an organization and helps create a more consistent understanding between different business units regarding the company's aspirations and capabilities, as well as helping create informal networks as employees build relationships in different departments.

Instilling accountability

The second distinctive symptom of a siloed culture is the tendency for employees to believe a given problem or issue is someone else's responsibility, not their own. Companies can counter this by institutionalizing mechanisms to help support cross-functional collaboration through flexibly deployed teams. That was the case at ING, which, because it identifies more as a technology company than a financial-services company, has turned to tech firms for inspiration, not banks. Spotify, in particular, has provided a much-talked-about model of multidisciplinary teams, or squads, made up of a mix of employees from diverse functions, including marketers, engineers, product developers, and commercial specialists. All are united by a shared view of the customer and a common definition of success. These squads roll up into bigger groups called tribes, which focus on end-to-end business outcomes, forcing a broader picture on all team members. The team members are also held mutually accountable for the outcome, eliminating the "not my job" mind-set that so many other organizations find themselves trapped in. While this model works best in IT functions, it is slowly making its way into other areas of the business. Key elements of the model (such as end-to-end outcome ownership) are also being mapped into more traditional teams to try to bring at least pieces of this mind-set into more traditional companies.

Start by finding mechanisms, whether digital, structural, or process, that help build a shared understanding of business priorities and why they matter. Change happens fast and from unpredictable places, and the more context you give your employees, the better they will be able to make the right decisions when it does. To achieve this, organizations must remove the barriers that keep people from collaborating, and build new mechanisms for cutting through (or eliminating altogether) the red tape and bureaucracy that many incumbents have built up over time.

Cultural changes within corporate institutions will always be slower and more complex than the technological changes that necessitate them. That makes it even more critical for executives to take a proactive stance on culture. Leaders won't achieve the speed and agility they need unless they build organizational cultures that perform well across functions and business units, embrace risk, and focus obsessively on customers. 

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